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Bill Yeomans, Interim Financial Services Director
 City of Burbank
 Burbank, California

In planning and performing our audit of the basic financial statements of the City of Burbank (City) as of and for the year ended June 30, 2009, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

However, we noted certain matters involving the internal control structure and its operation where improvements could be made. We offer the following recommendations for consideration by the City to strengthen its internal control structure.

(1) Improvement in the Cash/Bank Reconciliation Process

During our comparison of the City's cash and investments by institution to cash and investments by fund at June 30, 2009, we noted a material variance. Upon investigation of the variance, we found three adjustments totaling \$3.5 million for errors noted in the cash reconciliation process that were not recorded by the Finance Department at June 30, 2009. The cash reconciliation prepared by the Finance Department also contained certain immaterial unaccounted for variances that were not investigated and corrected. Additionally, the bank reconciliation prepared by the Treasury Department contained errors because it was performed at an interim date instead of June 30, 2009.

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(1) Improvement in the Cash/Bank Reconciliation Process, (Continued)

Recommendation

The cash and bank reconciliation process is an important control to ensure the City's cash and investments are properly accounted for. When the Finance Department detects errors in the cash reconciliation process, adjustments need to be made to the City's accounting records to correct those errors. All variances, whether material or not, should be investigated and corrected. Additionally, the Treasury Department should perform bank reconciliations on the last day of the month to eliminate additional reconciliations that need to be performed by the Finance Department for the period of time between the Treasurer's bank reconciliation and the end of the month.

(2) Close out of Capital Projects

During our review of the City's Construction in Progress, we noted several material projects that had been completed but were still included in Construction in Progress. Once a project is completed, it needs to be closed out and moved to a Capital Asset account, which starts the depreciation process. When projects are not moved to Capital Assets, the City understates the current year depreciation expense and accumulated depreciation.

Recommendation

At least once a year, the City's Finance Department should meet with the Public Works Department and project engineers to determine the status of each project included in construction in progress. If the project is "in service", it is required to be transferred to a capital asset and begin the depreciation process.

Additionally, many City projects, particularly street projects, involve the replacement or rehabilitation of an existing asset. The City needs to evaluate each closed project to ensure that the related capital asset deletion has been recorded in the accounting system.

(3) Adjustments Detected by the Audit Process

Paragraph 19 of the Statement on Auditing Standards No. 112 requires that the auditor identify material audit adjustments in the auditor's report on internal controls. For the year ended June 30, 2009, material adjustments detected by the audit process included adjustments to cash and investments as noted above, correcting principal and interest expenses on the 2003A PFA Golden State bonds, and reclassifying expenditure recorded for the purchase of a parking structure. The audit process also detected several immaterial audit adjustments.

Recommendation

An important element of controls over financial reporting is for management to identify adjustments necessary for financial statements to be fairly stated. Whenever possible, adjustments should be reflected in the accounting records prior to the start of the audit. When this is not possible, management should identify and communicate to the auditors the potential areas of adjustments that may need to be addressed during the audit process. This is an important element of internal control to reduce the risk of material misstatement.

(4) Formalization of Fraud/Ethics Policy

While making inquiries with management as required by the *Audit Risk Standards*, it was noted that the City does not have a formalized all-encompassing fraud policy. A formal fraud policy can be an effective method of communicating and reinforcing an antifraud culture within the City. A fraud policy communicates to all employees the City's position and policy on matters such as the following:

- Risks that the City faces from fraud, abuse, and other forms of misconduct;
- An ethical code of conduct;
- Definitions of ethical misconduct, including fraud and abuse;
- Employee's responsibility to report suspected ethical misconduct (including an established reporting mechanism, such as a member of the City Council, a designated member of City management, a hotline service, etc.);
- Organizational responsibility to investigate; and
- Disciplinary action for violations.

Recommendation

Internal control standards recommend that organizations develop and implement a formal fraud policy. We recommend that the policy be acknowledged and signed by each employee upon his or her hire date, in conjunction with an orientation that includes an emphasis on ethical conduct. Some organizations also require that employees sign a copy of the policy on an annual basis as evidence of their reaffirmation that they understand the policy and have complied with its provisions. In addition, the City could conduct fraud control training for all employees, not just new employees, and release a periodic message from the City Manager stressing the importance of ethical conduct. We recommend that the City implement procedures that are believed to be appropriate for its size and structure.

This letter is intended solely for the information and use of the City of Burbank's management, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Margaret Hoffman McCann P.C.

Irvine, California
November 13, 2009